



**TÜRKİYE CUMHURİYET
MERKEZ BANKASI**

Briefing on Inflation Report 2015-III

Erdem BAŞÇI
Governor

30 July 2015
Ankara

Inflation Report: Main Sections

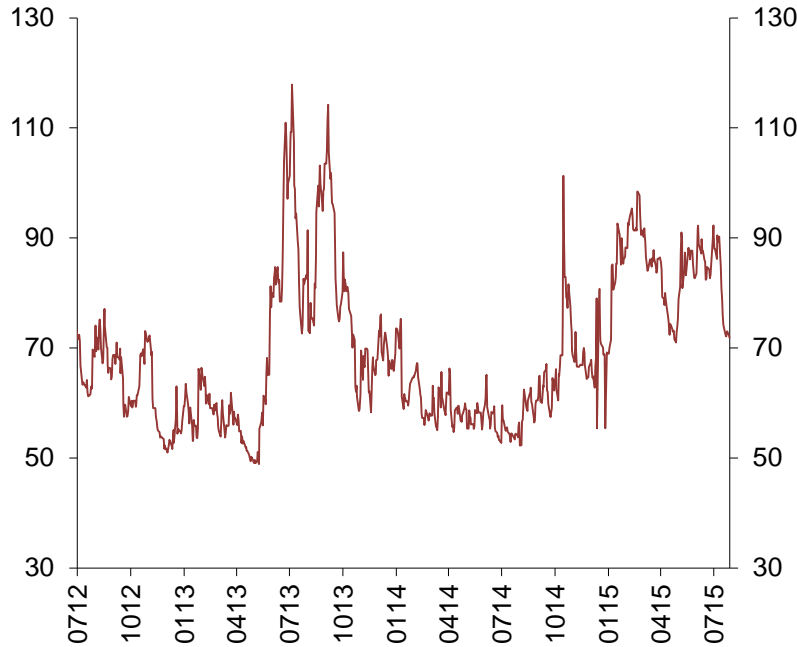
- Overview
- International Economic Developments
- Inflation Developments
- Supply and Demand Developments
- Financial Markets and Financial Intermediation
- Public Finance
- Medium Term Projections

2015 July Inflation Report: Boxes

- Information Content of Credit in Explaining Inflation
- Firm Strategy, Consumer Behaviour and Taxation in Turkish Tobacco Market
- Exploring the Relationship between Inflation and Exports in Food Items
- Use of Survey Data in Short-Term GDP Forecasts
- The Effect of Crude Oil Prices on Exports
- Government Spending Multiplier

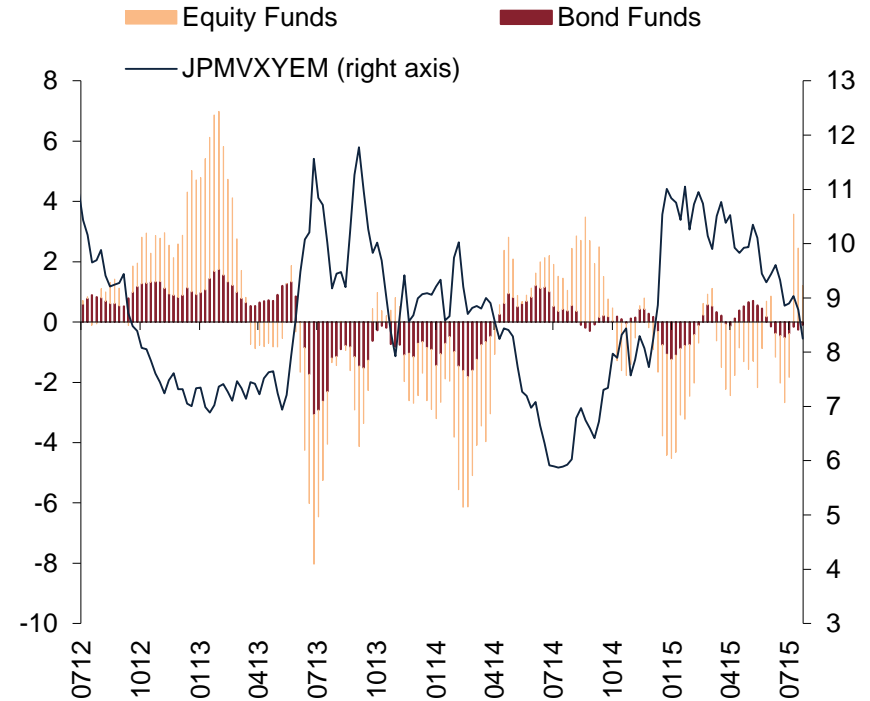
Global Uncertainties and Portfolio Flows

US Interest Rate Volatility Index (MOVE Index)
(Basis Points)



Source: Bloomberg.

Portfolio Flows to Emerging Economies
(4-Week Moving Average, Billion USD)
and Currency Volatility Index (JPMVXYEM) (Percent)



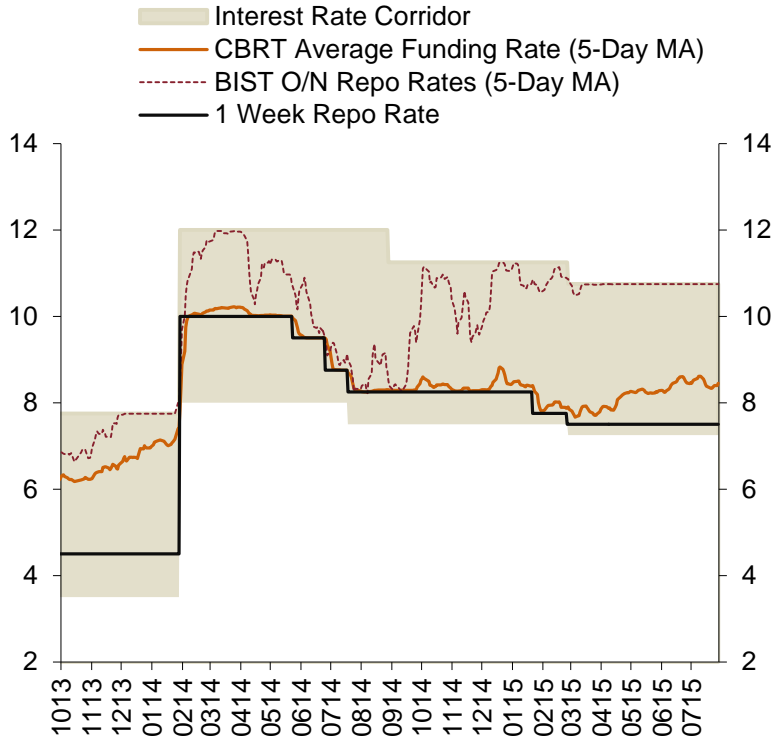
Source: EPFR, Bloomberg

- Volatility in long term rates of developed countries has reached high levels. Consequently, portfolio flows have been weak.

Monetary Policy and Financial Conditions

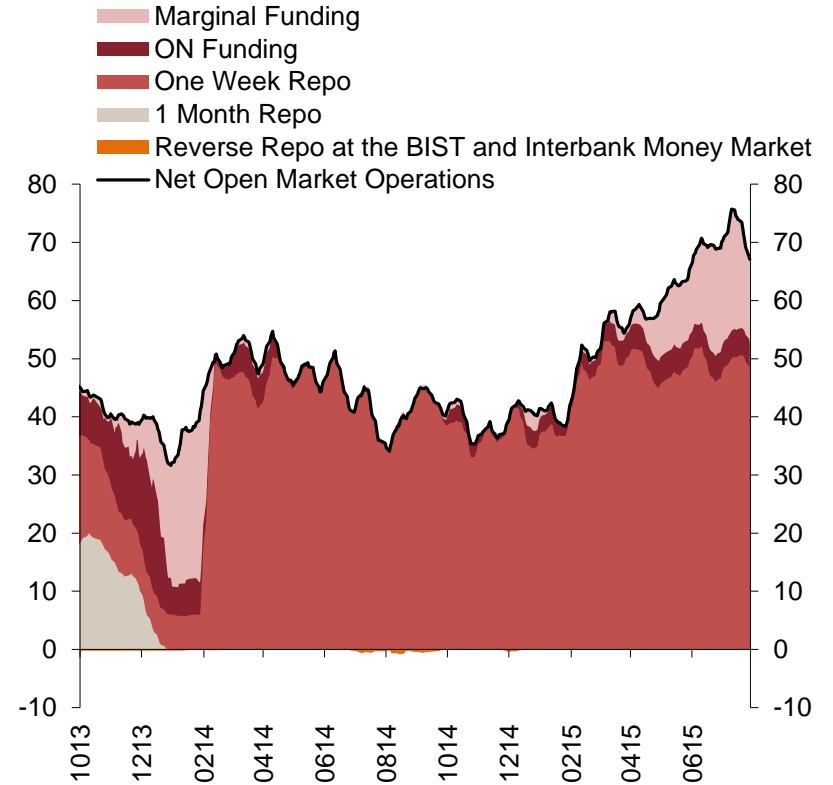
Monetary Policy

CBRT Rates and BIST Interbank O/N Repo Rates
(Percent)



Source: BIST, CBRT.

CBRT Funding*
(2-Week Moving Average, Billion TL)



*Marginal funding is O/N funding quoted at the upper limit of the corridor.

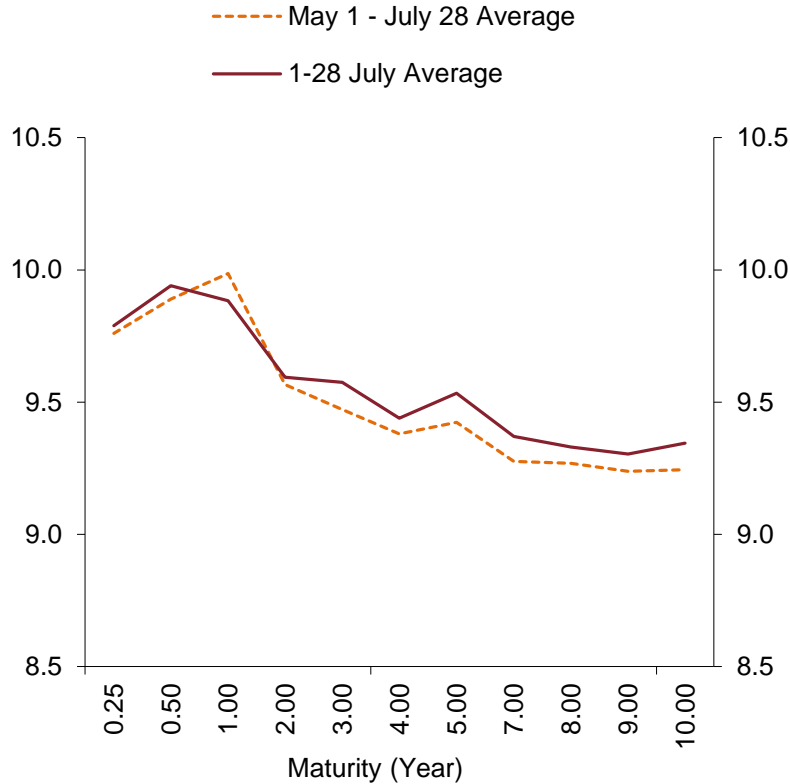
Source: BIST, CBRT.

➡ CBRT maintains a cautious monetary policy stance to achieve the price stability objective.

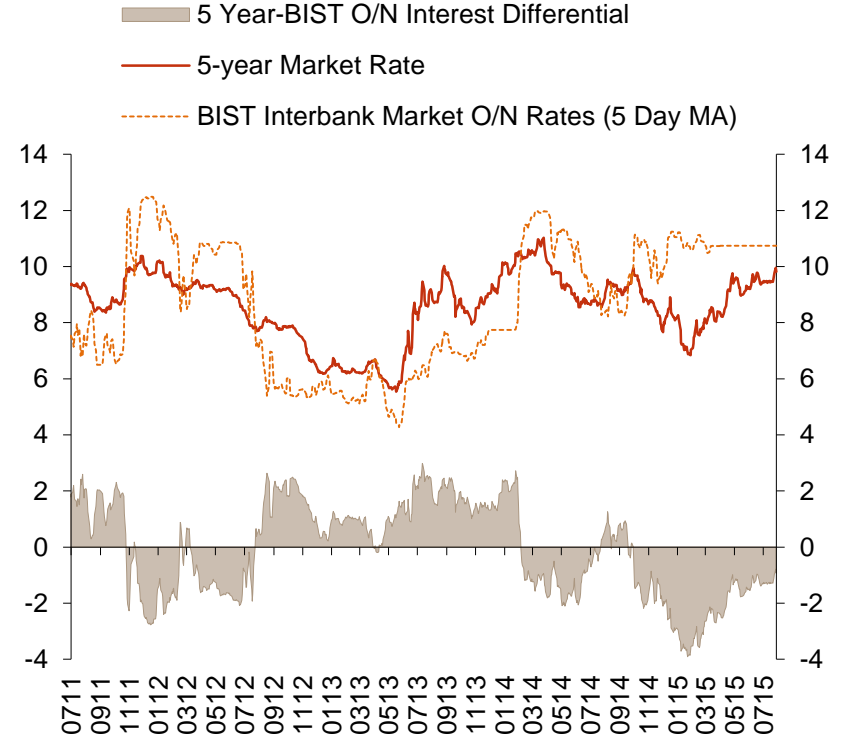
Monetary Conditions

Money Market Rates
(Percent)

Yield Curve
(Percent)



Source: Bloomberg.

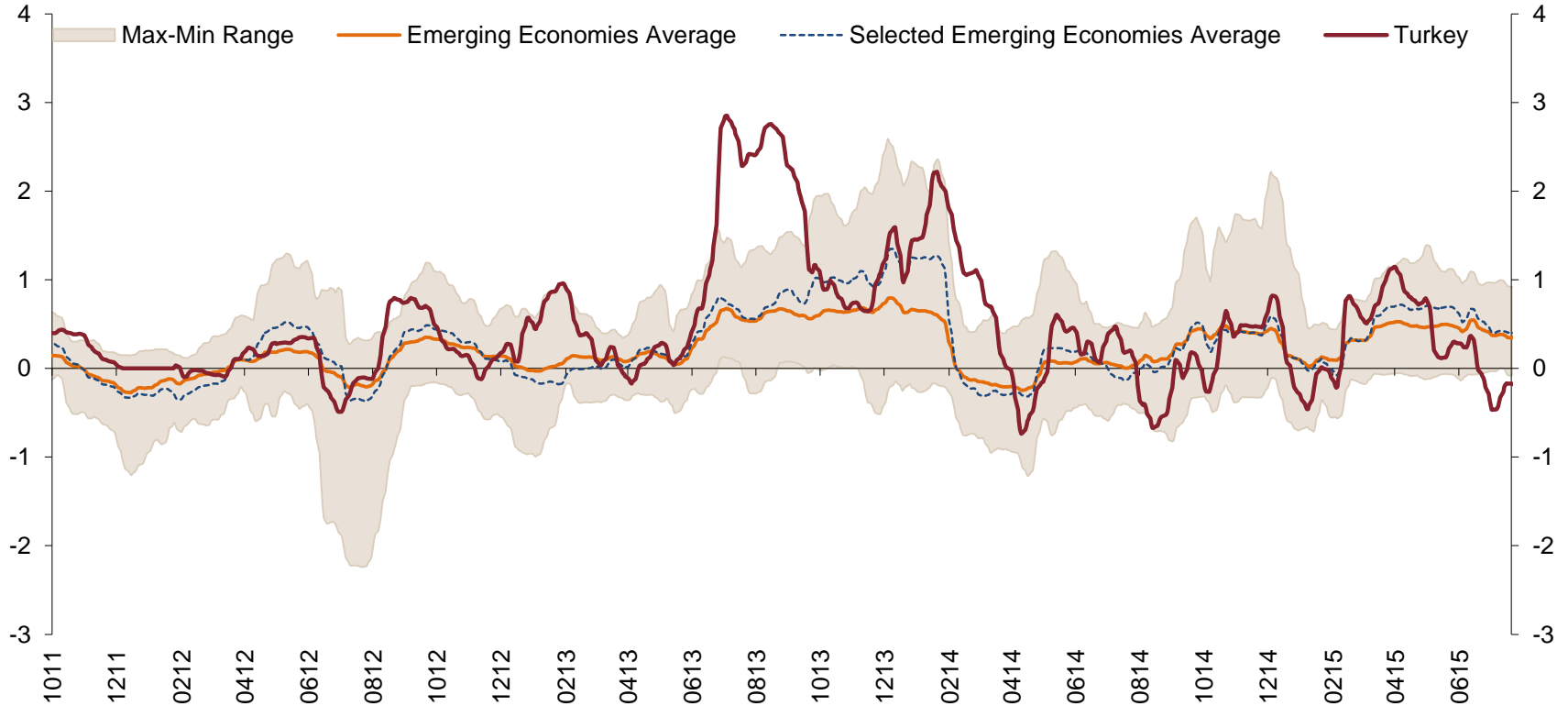


Source: BIST, CBRT, Bloomberg.

➡ Slope of the yield curve reflects the tight liquidity policy of CBRT.

Sensitivity to Global Interest Rate Shocks

Regression Coefficient of EM 10-Year Interest Rate on US 10-Year Interest Rate
(Weekly Changes, 60-Days Moving Window, 5 Day Moving Average)

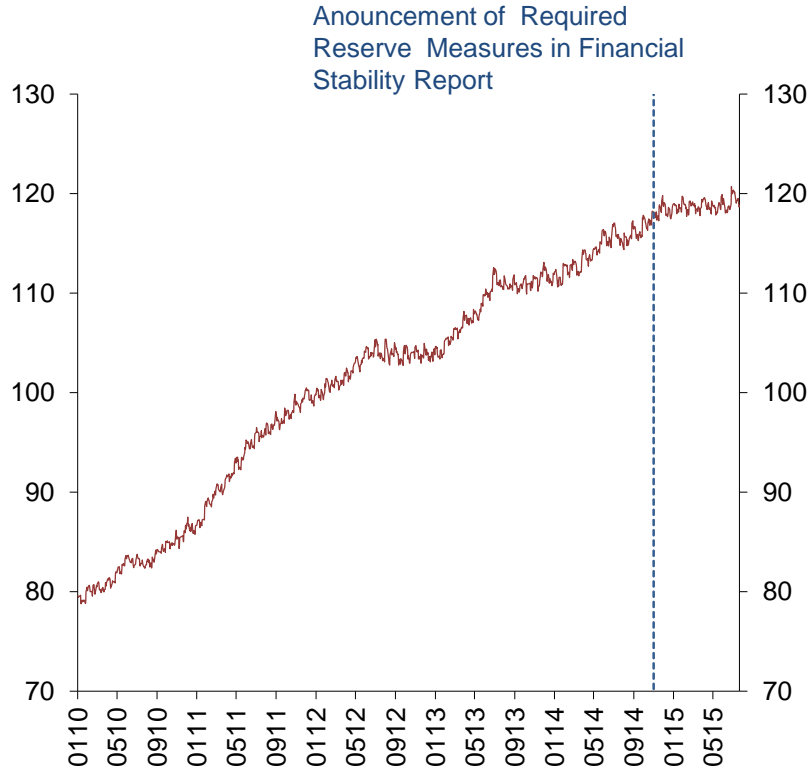


EM Sample: Brazil, Chile, Hungary, Poland, Peru, S. Africa, Mexico, Malaysia, Columbia, China, South Korea, India, Israel, Romania, Indonesia, Czech R., Thailand and Philippines. Selected EM: Brazil, S. Africa, India, Indonesia. Regression: $\Delta EM10YearRate = \beta_0 + \beta_1 * \Delta USD10YearRate$

- After the strong monetary policy tightening in January 2014, global interest rates have been significantly less influential on domestic markets.

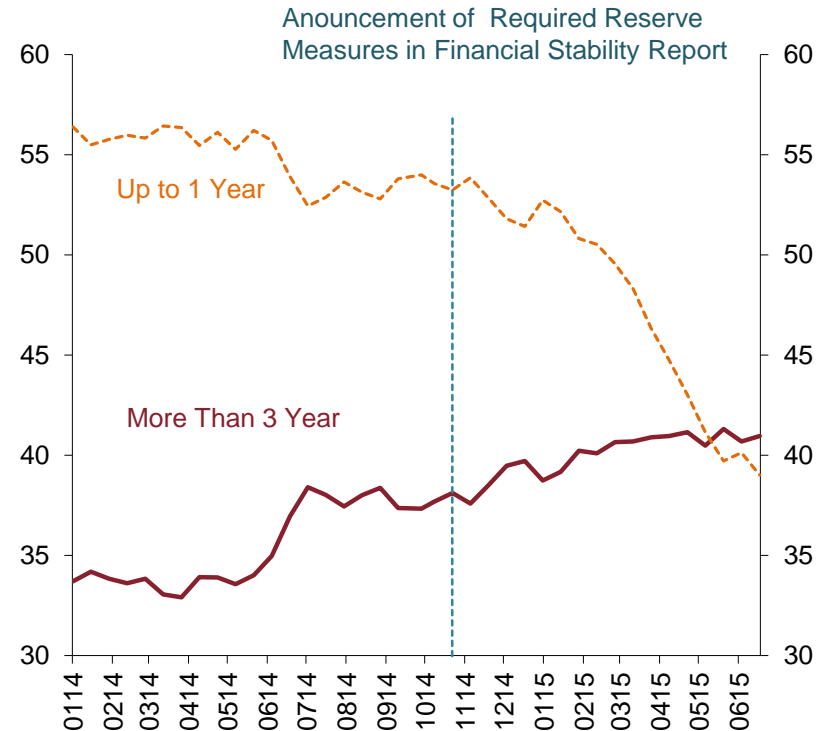
Financial Stability

Credit/Deposit
(Percent)



Source: CBRT.

Maturities of Non-Deposit Liabilities
(Percent)



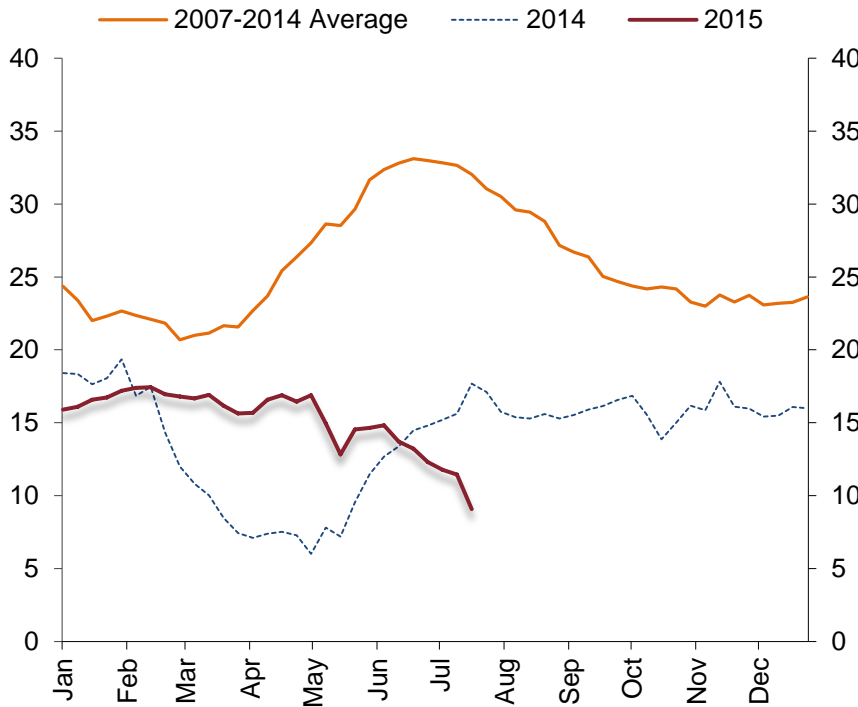
Source: CBRT.

- The measures implemented recently to support the FX liquidity, core liabilities, and long-term borrowing have enhanced the resilience of the economy.

Financial Stability

Consumer Loan Growth

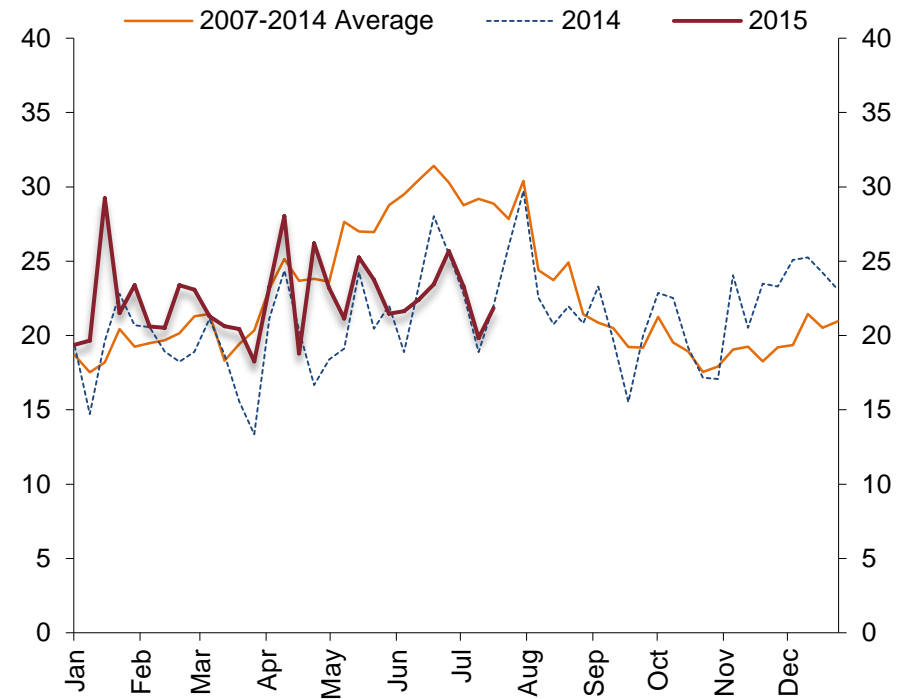
(13-Week Moving Average, Annualized, Percent)



Source: CBRT

Commercial Loan Growth

(13-Week Moving Average, Adjusted for Exchange Rate, Annualized, Percent)



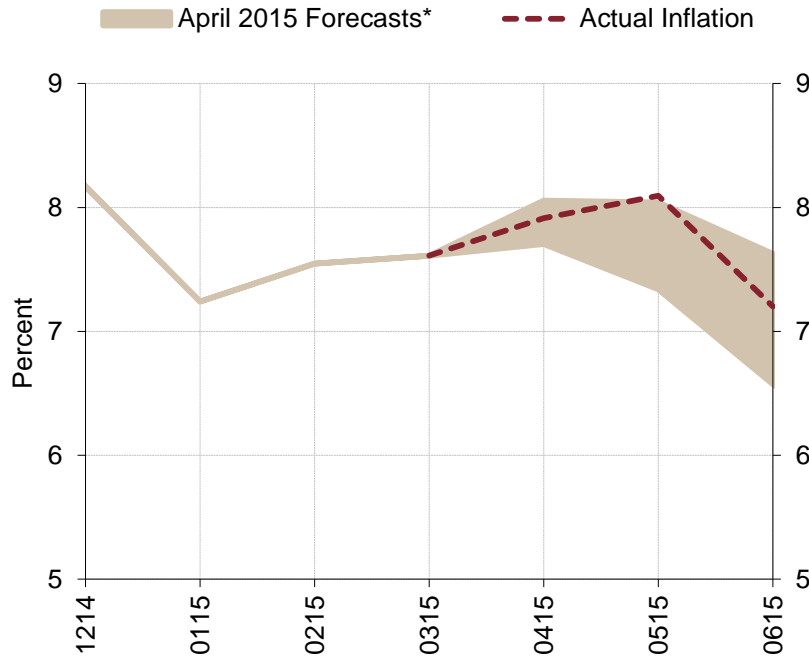
Source: CBRT.

- Commercial loans grow at a faster pace than consumer loans which has a favorable impact on price stability, financial stability and rebalancing.

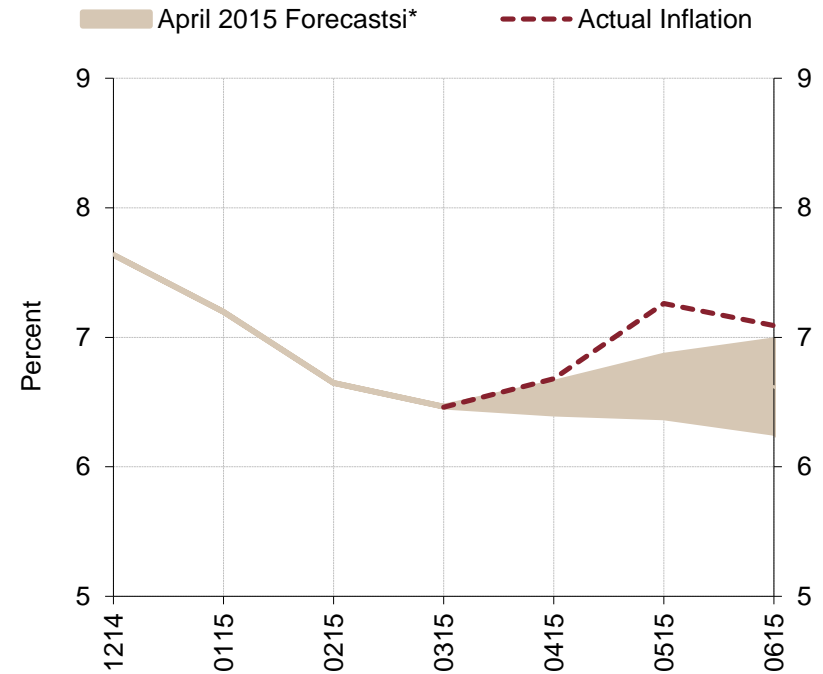
Macroeconomic Developments and Main Assumptions

April Inflation Report Forecasts and Realizations

April Inflation Forecasts and Realizations
(Percent)



April Inflation Forecasts and Realizations
Excluding Unprocessed Food and Tobacco
(Percent)



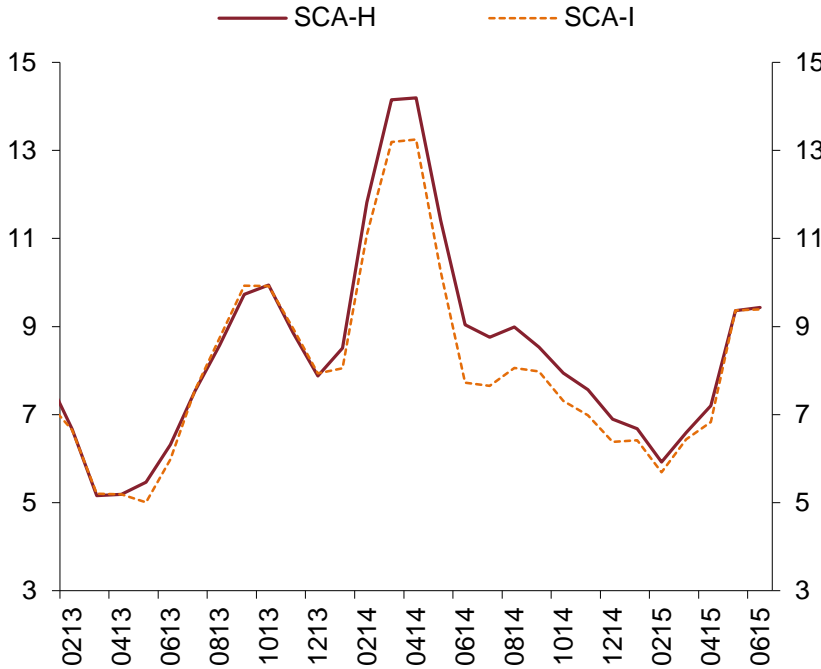
* Shaded region indicates the 70 percent confidence interval for the forecast.
Source: TURKSTAT, CBRT.

- Inflation at the end of the second quarter of 2015 was close to April Inflation Report forecast, while core inflation remained above the forecast.

Inflation

Core Inflation Indicators SCA-H and SCA-I

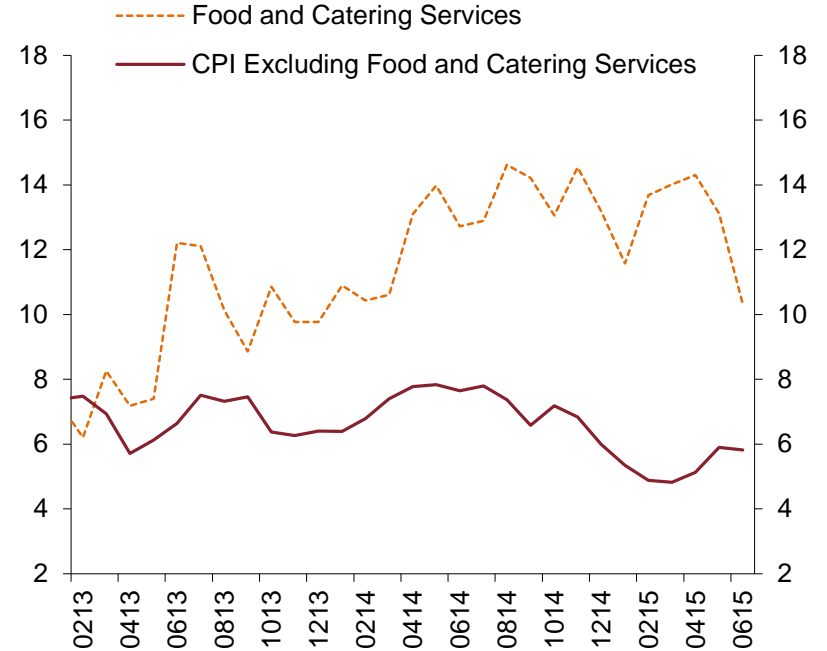
(Seasonally Adjusted, Annualized 3 Month Average,
Annual Percentage Change)



Source: TURKSTAT, CBRT.

Food and Non-Food Prices

(Annual Percentage Change)



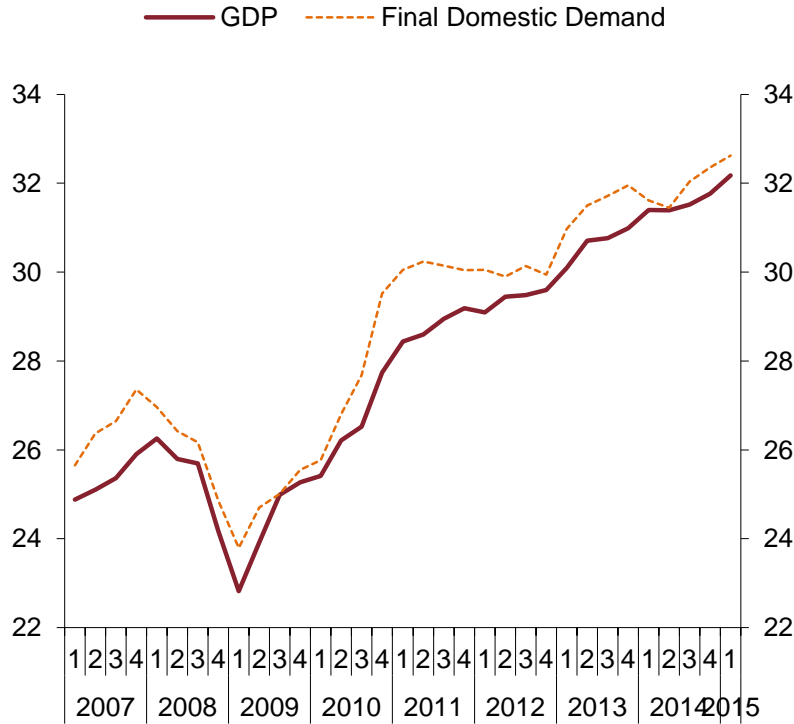
Source: TURKSTAT, CBRT.

- While the decline in food prices was the main source of the improvement in inflation in the second quarter, core inflation increased mainly due to exchange rate developments.

Aggregate Demand Developments

GDP and Final Domestic Demand

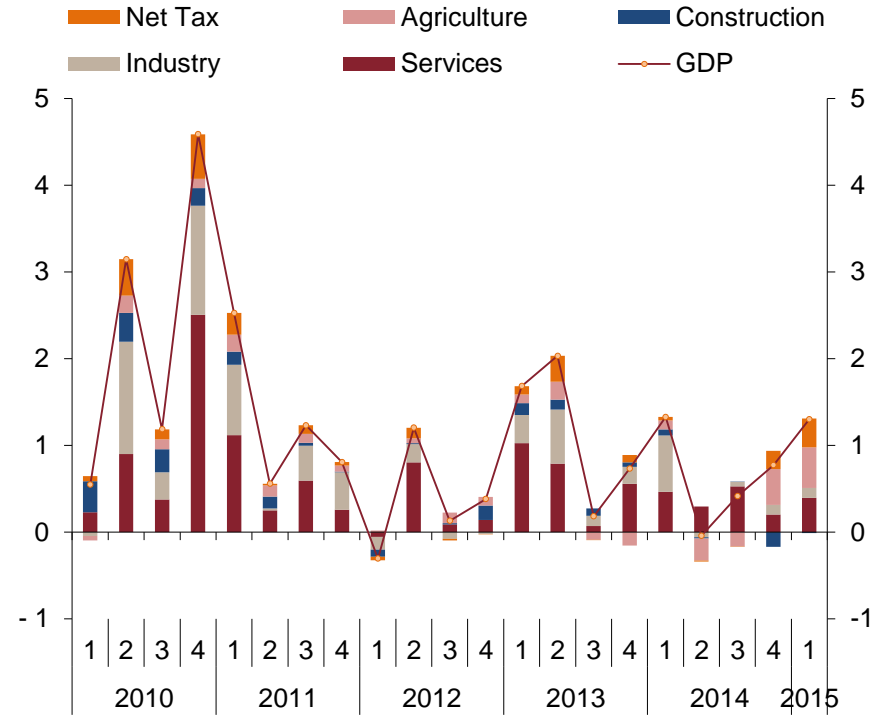
(Seasonally Adjusted, Billion TL, 1998 Prices)



Source: TURKSTAT, CBRT.

Contribution of Production Components to Year-on-Year GDP Growth

(Percentage Point)



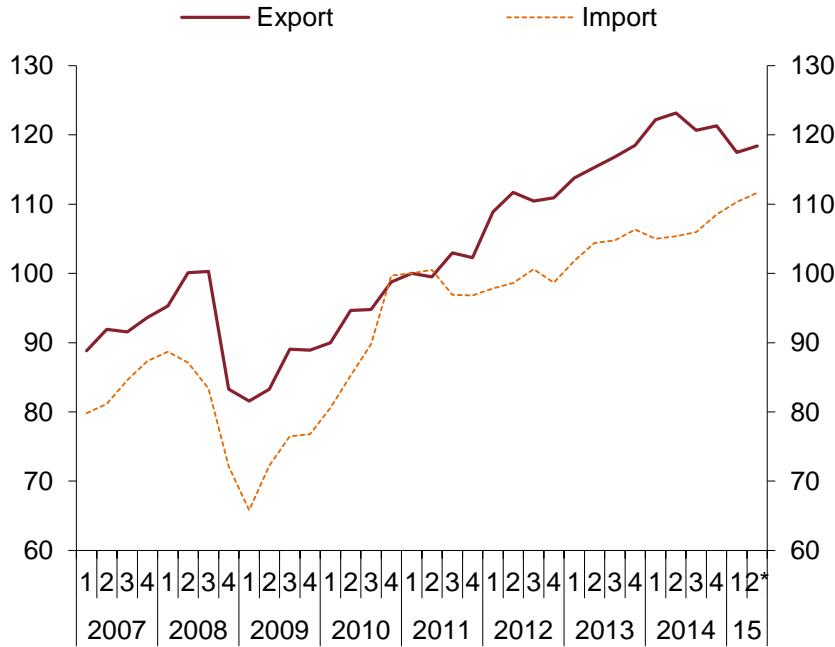
Source: TURKSTAT, CBRT.

➡ Economic activity continues to grow at a moderate pace.

External Balance

Import and Export Quantity Indices Excl. Gold*

(Seasonal Adjusted, 2011q1=100)

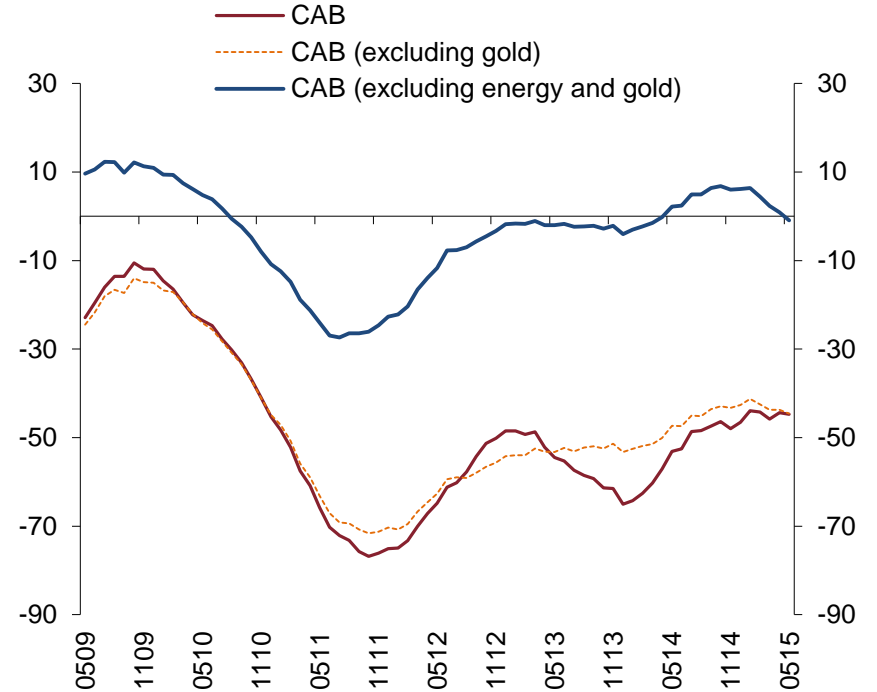


*April-May 2015

Source: TURKSTAT , CBRT.

Current Account Balance (CAB)

(12-Month Cumulative, , Billion USD)

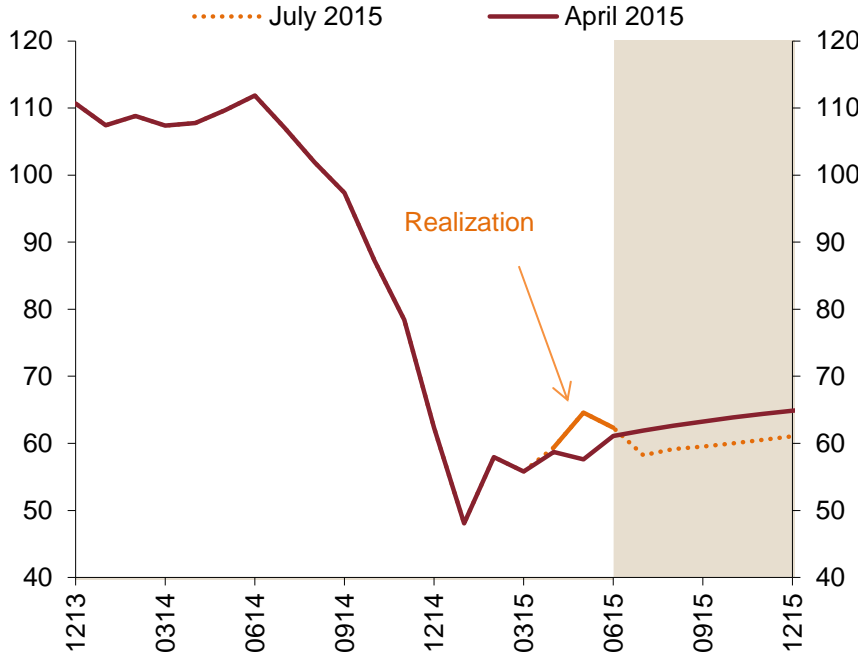


Source: TURKSTAT , CBRT.

- Despite the weak external demand, improvement in terms of trade and lower growth rate of consumer loans support the improvement in current account balance.

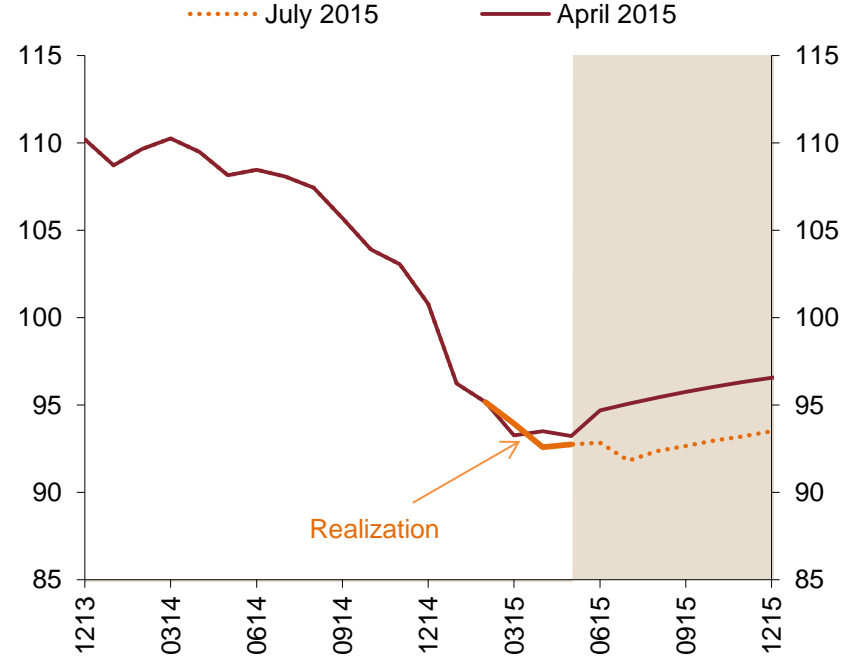
Oil and Import Prices

Oil Prices*
(USD/barrel)



* Shaded area indicates the forecast horizon.
Source: Bloomberg, CBRT.

Import Prices*
(USD, 2010=100)



* Shaded area indicates the forecast horizon.
Source: TURKSTAT, CBRT.

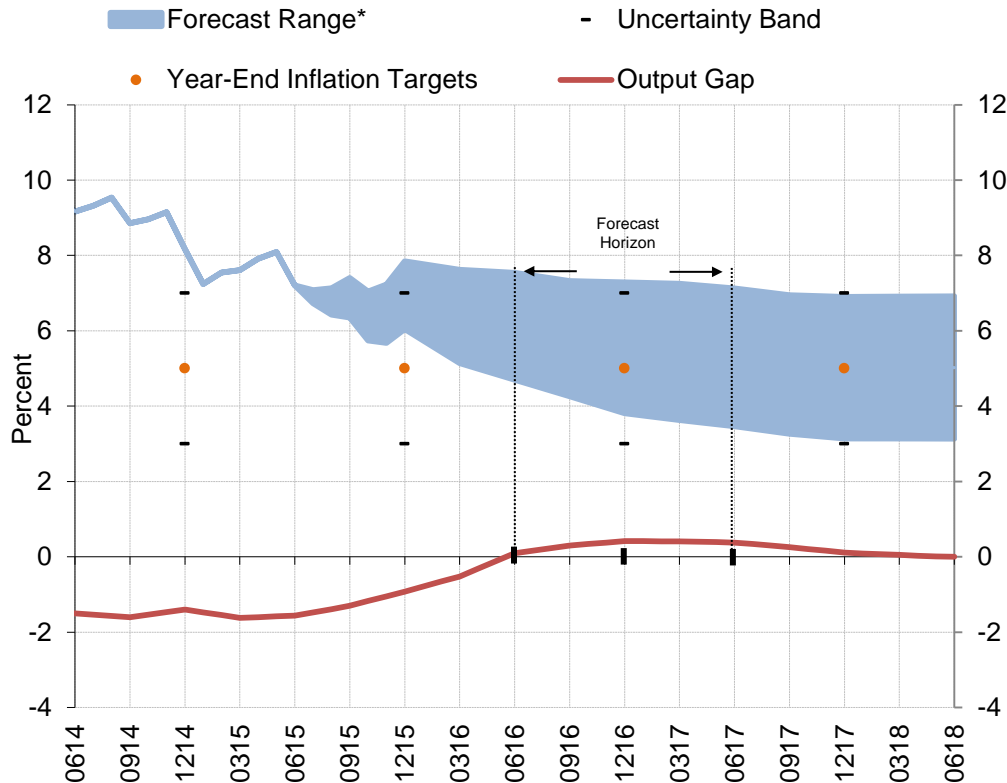
➡ In the second quarter of the year, oil prices remained above the path envisaged in the April Inflation Report while the import prices remained below.

Monetary Policy Stance

- Medium-term forecasts are based on the framework that cautious monetary policy stance will be maintained by keeping the yield curve flat until there is a significant improvement in the inflation outlook.
- It is assessed that the annual loan growth rate will continue to hover around its recent reasonable level in 2015, also thanks to the macroprudential measures.

Inflation Outlook

Inflation and Output gap Forecasts



*Shaded region indicates the 70 percent confidence interval for the forecast.

Accordingly, inflation is expected to

- be between 6.0 % and 7.8 % (mid-point of 6.9 %) by the end of 2015,
- be between 3.7 % and 7.3 % (mid-point of 5.5 %) by the end of 2016,
- stabilize at 5 % in the medium term

with 70 percent probability.



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